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Nos. 82-34 and 82-226

IN THE

# Supreme Court of the United States

OCTOBER TERM, 1982

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AMERICAN PAPER INSTITUTE, INC., *Petitioner*

v.

AMERICAN ELECTRIC POWER SERVICE CORPORATION, *et al.*

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FEDERAL ENERGY REGULATORY COMMISSION, *Petitioner*

v.

AMERICAN ELECTRIC POWER SERVICE CORPORATION, *et al.*

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**On Writs Of Certiorari To The United States Court Of Appeals For The District Of Columbia Circuit**

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## BRIEF FOR RESPONDENT ELIZABETHTOWN GAS COMPANY IN SUPPORT OF PETITIONERS

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## BRIEF FOR RESPONDENT ELIZABETHTOWN GAS COMPANY IN SUPPORT OF PETITIONERS

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Elizabethtown Gas Company ("Elizabethtown"), intervenor in the court below, filed a brief in support of the petition for writ of certiorari in No. 82-34. Elizabethtown here urges the Court to grant the relief sought by petitioners in both captioned cases.

## PRELIMINARY STATEMENT

Elizabethtown is a public utility organized and existing under the laws of the State of New Jersey.[1] Under regulation by the New Jersey Board of Public Utilities, Elizabethtown engages in the sale and distribution of gas in 68 municipalities serving over 190,000 customers. Elizabethtown competes in its service area with electric utilities supplying the energy needs of residential, commercial and industrial end users.

Elizabethtown is an actual supplier of gas to cogeneration facilities and a potential supplier of gas to cogeneration facilities which could qualify for the benefits of the Public Utility Regulatory Policies Act of 1978 ("PURPA"), Pub.L. No. 95-617, 92 Stat. 3117.[2]

Petitioners challenge the decision of the court below insofar as it vacated two of the rules set out in Federal

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[1] Elizabethtown is a subsidiary of National Utilities & Industries Corporation and has as affiliates Achter Kol Corporation, National Computer Utility Company, Enercorp Resources, Inc., Utility Propane Company, National Gas Gathering Company, National Energy Leasing Company, National Enerdrill Corporation, and The Lenape Resources Corporation.

[2] The relevant provisions of PURPA are reproduced on pages A-7 to A-19 of Appendix A to the petition for writ of certiorari in No. 82-34. Section 201 of PURPA required the Federal Energy Regulatory Commission to establish criteria under which cogeneration and small power production facilities could qualify for PURPA benefits. The Commission's Order No. 70, as amended, setting forth those criteria is not before this Court. The text of Order No. 70 is reproduced on pages B-120 to B-199 of Appendix B to the petitition in No. 82-34.

Energy Regulatory Commission ("FERC") Order No. 69 which implemented Section 210 of PURPA.[3]

Elizabethtown accepts, for purposes of this brief, Petitioners' statements of questions presented, lists of parties to the proceeding below, statements of opinions below, statements of jurisdiction, lists of statutory and regulatory provisions involved, and statements of the case.

## SUMMARY OF ARGUMENT

Cogeneration facilities are ordinarily far more fuel-efficient than are public utility steam electric power generating plants. Such cogeneration facilities can provide a decentralized, competitive source of bulk electric power for local distribution at a time of rising electric bills. They can create a competitive market for sellers of fuels utilizable in cogeneration facilities.

The construction of cogeneration facilities has been stifled by the lack of assured outlets at reasonable prices for the surplus power they generate. The two rules nullified by the lower court helped overcome that handicap. Under those rules electric utilities were required to interconnect with qualifying cogeneration facilities, and to pay a price for surplus power which is no higher than their full avoided costs of electric energy from other sources.

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[3] Section 210(a) directed the Commission to prescribe rules which it deemed necessary to establish relationships between qualifying facilities and electric utilities "to encourage cogeneration and small power production". 16 U.S.C. § 824a-3(a). Order No. 69, as amended, implementing this provision, is reproduced on pages B-38 to B-119 and B-175 to B-199 of Appendix B to the petition in No. 82-34.

Unless the rules are reinstated, the purpose of Section 210(a) of PURPA "to encourage cogeneration and small power production" will be frustrated.

## ARGUMENT

1. It is more efficient to use fossil fuels in a cogeneration unit than to use them in a typical public utility electric power generating plant. This is because the steam utilized in the latter is condensed after passing through the electric-generating turbines instead of being put to some other industrial or commercial use. The Commission found: "Cogeneration facilities use significantly less fuel to produce electricity and steam (or other forms of energy) than would be needed to produce the two separately."[4]

The fact that the distribution of electricity must be a monopoly does not mean that the generation, transmission and distribution functions in the industry must be vertically integrated, or that competition is not possible at the generation level.[5]

Historically, monopoly at the generation level has been fostered by technical characteristics of the utility industry: huge quantities of capital in long-lived and inflexible facilities directly connected to consumers and the ex-

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[4] Commission Order No. 69, page B-39 of Appendix B to petition in No. 82-34. A further benefit expected from cogeneration plants is reduced transmission losses due to the proximity of the plant to the load center utilizing the electricity. (R. 2292)

[5] *Otter Tail Power Co.* v. *United States*, 410 U.S. 366 (1973). See 2 A. Kahn, *The Economics of Regulation: Principles and Institutions* 18-19 (1971); Meeks, "Concentration in the Electric Power Industry: The Impact on Antitrust Policy," 72 *Colum. L.Rev.* 64, 82 (1972).

istence of substantial economies of scale in the bulk power plants.[6] In recent years, costs of constructing generation facilities have been increasing faster than the general level of inflation, causing unit costs and rates to increase steadily.[7]

Cogeneration facilities offer a modest antidote to this trend. They involve relatively small outlays of capital, by persons outside the public utility industry. They offer much more economic use of fuel in an economy which has seen fuel costs of electric utilities push rates to very high levels.

The Commission's rulemaking program might result in the construction of 12,000 MW of new capacity by qualifying facilities by 1995. This could cause electric utilities to defer or cancel construction of eleven 500 MW coal-fired steam plants, one 1,000 MW nuclear plant, a number of 75 MW gas turbines, and certain large scale hydro and combined cycle installations. The environmental consequences of constructing and operating these plants could be avoided.[8]

About 25 percent of the PURPA-induced cogeneration in the *industrial* sector is expected to be installed in the Middle Atlantic area which includes New Jersey. The

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[6] See Bonbright, J., *Principles of Public Utility Rates* 8-17 (1961).

[7] U. S. Department of Energy, *The National Power Grid Study*, Vol. 1, Final Report, DOE/ERA-0056-1, pp. 22-23 (1980). Approximately two-thirds of the capital outlays of electric utilities is attributable to the construction of generation facilities; up from forty percent in the mid 1960's. This dramatic shift is due to a very rapid rise in construction costs and delays in construction schedules. *Id.* at 18, 54.

[8] Order No. 70, page B-140 of Appendix B to petition in No. 82-34.

three largest industrial segments likely to participate in PURPA-induced cogeneration are the pulp and paper, chemical, and petroleum refining industries. The chemical industry anticipates using natural gas in gas-fired combustion turbines and, with process-derived fuels, in steam-topping cycle engines. Pulp and paper plants would use gas and oil as fuel for cogeneration to augment wood and other process by-products.[9]

PURPA-induced *commercial* cogeneration is expected to occur almost exclusively in the Middle Atlantic area and to take the form primarily of diesel engines and dual-fuel engines. Natural gas would be used in dual-fuel use engines when available and less expensive than diesel fuel.[10]

Gas distribution companies indicated during the rulemaking process an interest in supplying PURPA-induced cogeneration.[11] Efforts by the electric utilities to prevent the use of natural gas in such facilities were rejected by the Commission and by the Court of Appeals.[12]

The cogeneration rules were intended to provide competitive cogeneration sources for bulk electric power. The Commission found: "By obtaining electric energy from cogeneration and small power production, utilities

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[9] R. 2292.

[10] *Ibid.*

[11] R. 389-390, 712-719, 1412-1430, 2317-2319.

[12] *American Electric Power Service Corp.* v. *Federal Energy Regulatory Commission*, 675 F.2d 1226, 1241-5 (D.C. Cir. 1982), *reh. denied*, 675 F.2d at 1246.

can reduce the burning of fuel and construction of plants than would otherwise be required."[13]

2. The installation of fuel-efficient cogeneration facilities has been stultified because of the lack of assured interconnections with electric utilities which might serve as a market for surplus electric power from the cogeneration facility, and a pricing mechanism for surplus power which would facilitate the economic planning of new cogeneration facilities.[14]

Those considering the installation of cogeneration facilities in industrial plants and at commercial sites are not in the business of generating electricity for public consumption. Decisions as to the type of facilities to be installed and the fuel to be used are governed by manufacturing and commercial concerns which cannot await the uncertain outcome of drawn-out litigation with electric utilities in the administrative arenas. The prospect of traversing an assuredly expensive and possibly barren path through the administrative agency/court maze, should they choose the cogeneration option, is enough to effect rejection of that business choice.

If cogeneration is to be encouraged as a source of bulk electric power for the public, as we submit Congress intended in enacting PURPA, then access to the electric distribution systems must be simple and the economics of that course certain. Those objectives cannot be achieved without reversing the court below.

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[13] R. 1217.

[14] Commission Order No. 70, page B-121 of Appendix B to petition in No. 82-34.

Consolidated Edison Company of New York, Inc., petitioner in the court below, serves with electricity a territory The Brooklyn Union Gas Company serves with gas. None of the gas-fired cogeneration facilities in Brooklyn Union's territory was connected with Consolidated Edison's electric distribution system.[15] Brooklyn Union advised the Commission in the rulemaking proceeding:

> Among those parties most vociferously opposing the use of natural gas for "inferior" cogeneration purposes are electric utilities which are actively engaged in dissipating this nation's "gas bubble" by using gas as boiler fuel in the generation of electricity. In light of the efficiency standards which the Commission has proposed for gas-fired CFs [cogeneration facilities] which seek qualifying facility status, Brooklyn Union submits that the twin goals of conserving natural resources and maximizing fuel use efficiency could be better achieved by use of natural gas in CFs which meet the Commission's efficiency standards and the termination, at the *earliest possible date*, of programs which encourage or permit consumption of vast quantities of natural gas in comparatively inefficient utility central electric generating stations.[16]

The electric utilities successfully persuaded the court below to interpret PURPA in a way that needlessly suppresses opportunities for competition in the bulk electric power industry, where competition can and ought exist.[17]

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[15] R. 1413.

[16] R. 1418.

[17] See *Cantor* v. *Detroit Edison Co.*, 428 U.S. 579 (1976); *Otter Tail Power Co.* v. *United States*, *supra*; *Gainesville Utilities Department* v. *Florida Power and Light Co.*, 573 F.2d 292 (5th Cir. 1978), *cert. denied*, 439 U.S. 966 (1978).

If cogeneration is not used, a factory or commercial establishment would utilize a low-pressure steam boiler, or a furnace, to obtain its thermal requirements, and would purchase electricity from the local electric utility.[18] This results in a larger market for the electric utility's own bulk generation, rather than competition in meeting the bulk generation requirements of the utility.

3. "Section 210 of PURPA's Title II . . . seeks to encourage the development of cogeneration and small power production facilities." *Federal Energy Regulatory Commission* v. *Mississippi*, 102 S.Ct. 2126, 2132 (1982). Faced with an obligation to adopt rules encouraging the development of cogeneration, the Commission chose means which would accomplish that result. The lower court did not conclude otherwise.

One may well argue that there are better ways to accomplish that legislative end, ones that are more "fine-tuned" in terms of the concerns of the electric utilities. But that is a proper matter for agency discretion. Although the inquiry "into the facts is to be searching and careful, the ultimate standard of review is a narrow one. The court is not empowered to substitute its judgment for that of the agency." *Citizens to Preserve Overton Park* v. *Volpe*, 401 U.S. 402, 416 (1971).

The Commission's rules were within the granted power, issued pursuant to the proper procedure, and have a reasoned basis. See *Bowman Transportation, Inc.* v. *Arkansas-Best Freight System, Inc.*, 419 U.S. 281, 285 (1974).

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[18] R. 2293.

## CONCLUSION

This court should hold that the two rules of the Commission, overturned by the Court below, are the product of reasoned judgment exercised within the ambit of the discretionary judgment delegated by Congress to FERC under PURPA and are valid.

Respectfully submitted,

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